

On December 31, 2007, the Commission issued a “Notice of Filing of Annual Compliance Report by the Postal Service and Solicitation of Public Comment,” requesting comments on the Postal Service’s FY 2007 Annual Compliance Report. The deadline for initial comments is January 30, 2008, and the deadline for reply comments is February 13, 2008. Valpak Direct Marketing Systems, Inc., and Valpak Dealers’ Association, Inc. (hereinafter “Valpak”) hereby submit these joint initial comments in response to the Commission’s Notice.

I. THE POSTAL SERVICE’S FIRST ANNUAL COMPLIANCE REPORT VIEWED ALONE DOES NOT PROVIDE SUFFICIENT INFORMATION TO THE COMMISSION OR MAILERS TO EVALUATE COMPLIANCE WITH PAEA OR TO ACHIEVE THE “INCREASED TRANSPARENCY” REQUIRED FOR THE RATEMAKING PROCESS.

A. PAEA’s Requirements for Annual Compliance Report

Under the PAEA, the requirements for the annual report for the prior year are:

- (1) which shall **analyze costs, revenues, rates, and quality of service**, using such methodologies as the Commission shall by regulation prescribe, and in sufficient **detail** to demonstrate that all products during such year complied with all applicable requirements of this title; and
- (2) which shall, for each **market-dominant** product provided in such year, provide—
 - (A) product information, including mail **volumes**; and
 - (B) measures of the **quality of service** afforded by the Postal Service in connection with such product, including—
 - (i) the level of service (described in terms of **speed of delivery and reliability**) provided; and
 - (ii) the degree of **customer satisfaction** with the service provided. [39 U.S.C. § 3652(a) (emphasis added).]

This reporting provision does not specify calendar year or fiscal year, but it is obvious that the Postal Service and the Commission have understood this to mean fiscal year. The Postal Service's fiscal year ends September 30, so its annual report to the Commission will be due no later than December 29 of every year.

Further, the reporting provision does not specify the first year for which the report should be filed. PAEA was enacted on December 20, 2006, and could have been read to require that a report be filed on December 29, 2006, but certainly no one anticipated that the first annual report would be filed at that time.

PAEA's description of what is required to be filed is broad and general, and it appears that Congress left to the Commission the responsibility to issue regulations which would flesh out the specific requirements for the Postal Service filing. For example, PAEA provides that the required analyses of "costs, revenues, rates, and quality of service" would be prepared and filed "in sufficient detail" and "using such methodologies as the Commission shall by regulation prescribe." 39 U.S.C. § 3652(a)(1).

On October 29, 2007, in Order No. 43, "Order Establishing Ratemaking Regulations for Market Dominant and Competitive Products" the Commission announced that it will begin a rulemaking for the annual compliance review "as quickly as practicable." Docket No. RM2007-1, Commission Order No. 43, p. 2. This year, however, despite the fact that the Commission has not yet issued such regulations, the Postal Service has taken the initiative and made its first filing, apparently seeking to provide at least the information required by the general requirements of PAEA, as set out above. And now, even in the absence of Commission regulations, the Postal Service FY 2007 Annual Compliance Report can be

evaluated for compliance with the specific requirements for the annual report set out in PAEA, *supra*, and with the requirement for increased transparency in the ratemaking process, discussed in section I. B. *infra*.

B. PAEA's Requirement for Increased Transparency

PAEA requires the Commission not just to maintain, but actually to “increase,” the “transparency of the ratemaking process.” 39 U.S.C. § 3622(b)(6). *See* Docket No. RM2007-1, Valpak Comments on Regulations Establishing a System of Ratemaking in Response to Commission Order No. 26 (Sept. 24, 2007), p. 6, and Valpak Reply Comments on Regulations Establishing a System of Ratemaking in Response to Commission Order No. 26 (Oct. 9, 2007), pp. 3-5.

When the Commission issued its rules on ratemaking, it recognized that PAEA called for “increased” transparency, but that the increase in transparency is to be achieved from all requirements of PAEA, rather than the ratemaking process alone. *See* Docket No. RM2007-1, Commission Order No. 43 (Oct. 29, 2007), pp. 17-19 (“The Commission is optimistic that the combination of [i] pre-implementation of rate changes, [ii] periodic reporting by the Postal Service, [iii] annual compliance reports by the Commission, and [iv] the complaint mechanism all supported by the Commission’s subpoena power, will serve to **increase** the level of transparency and accountability of postal rate setting under the PAEA relative to that which prevailed under the prior regulatory regime,” p. 18 (emphasis added)).

As the Commission correctly points out, the requirement of increased transparency was to be accomplished by the totality of Commission rulemakings.

1. However, it appears from Order No. 43 that “increased transparency” is not to be achieved primarily from [i] “pre-implementation of rate changes.”
2. The Commission’s regulations relating to [ii] “periodic reporting by the Postal Service” were issued under the authority of the Postal Reorganization Act of 1970 (“PRA”), well prior to the enactment of PAEA on December 20, 2006, and have not been amended since. *See* 39 C.F.R. § 3001.102. These regulations are still in effect and are being complied with by the Postal Service. When the Commission modifies the periodic reporting regulations, it could create “increased transparency,” but these matters are not now before the Commission.
3. It is highly unlikely that [iv] “the complaint mechanism” referred to above will be a principal source of “increased transparency,” as complaints probably cannot even be filed unless a certain amount of information is available through other methods of disclosure. Certainly, it would be unwise to rely primarily on a mailer-driven occasional complaint procedure for regular disclosure.
4. Therefore, it seems most likely that “increased transparency” will be achieved primarily through [iii] the “annual compliance” mechanism.

C. An Examination of the FY 2007 Annual Compliance Report

As a baseline, it seems useful to examine the Commission’s rules for what was formerly required under PRA for rate cases, and specifically what PAEA requires for the annual compliance report under section 3652, then compare those PRA and PAEA requirements vis-a-vis what the Postal Service actually has included in its FY 2007 Annual

Compliance Report. (It is recognized that this is a retrospective view and therefore elements of what were provided in prior rate cases — such as proposed rates — will be provided later with the Postal Service’s notice of a rate adjustment.)

An initial effort to make this comparison is set out in chart form in Appendix A. (Wherever a prior requirement seems to be rendered moot by the new law, the chart shows “N/A” for not applicable.) Although it has proven difficult to summarize and simplify this analysis in a chart, Appendix A indicates that the Postal Service has included in its Report those items specifically required by PAEA section 3652, but less than that which was submitted with prior rate cases. Furthermore, the Postal Service “emphasize[s] ... that the inclusion of information in this transitional Report does not necessarily mean that the Postal Service believes that such information should be included in future reports under the PAEA.” Postal Service Report, p. 2. This would appear to indicate that the Postal Service reserves the right to take the position that it has over-disclosed in this FY 2007 Annual Compliance Review.¹

D. The Commission’s Rules Should Require Additional Information to Be Filed in Future Annual Compliance Reports

It is understood that mailers will have an opportunity to comment on what the Postal Service should be required to file in future annual compliance reports when the Commission

¹ Such an argument by the Postal Service would not be unreasonable, of course. And the corollary is true, that just because mailers do not find fault with this transitional annual compliance report, they should not be precluded from commenting on proposed regulations requiring greater disclosure in the future. Also, even if the Commission finds the Postal Service’s Report and other filings sufficient in this docket, that should not preclude the Commission from requiring additional information in the future.

establishes a docket to write these rules. Nevertheless, the current filing may be considered a “dry run” in the sense that the Postal Service’s Report was issued without regulations, and rates being examined were not set under PAEA. If the Postal Service files this same information next year, however, neither mailers nor the Commission will be able to make a fully-informed determination of compliance.

Although it is true that Commission can seek more information (as it has done in Commission Information Request No. 1, Jan. 24, 2008), backed by its subpoena power (39 U.S.C. § 504(f)(2)), having requisite information available at the outset would enable the Commission and mailers to review the Postal Service’s future annual reports in a more timely manner. The Commission is limited to 90 days to make a determination of compliance. 39 U.S.C. § 3653(b). Mailers have been given an even shorter time to review the Postal Service filing and make comments. The Commission’s authority to order the Postal Service to remedy any noncompliance (*see* Section IV, *infra*) is conditioned on a “timely written determination of noncompliance.” 39 U.S.C. § 3653(c). Thus, the Commission’s future rules should require that sufficient information be filed with the annual report so as to reduce the amount of information the Commission would need to seek from the Postal Service during its review.

Lastly, although the Commission decided not to permit discovery in the context of Rate Change Notices, the Commission should consider allowing a period of discovery during its annual review for determination of compliance for commenters to seek further, relevant information. The unique perspective of intervenors in rate cases has led to many significant improvements in data, and has helped increase efficiency for the Postal Service. If an annual report (with supporting information) either does not contain necessary relevant information, or

is unclear, the Postal Service should be required to clarify such information or provide further information. Such discovery during an annual compliance review, backed by the Commission's subpoena power under section 504(f)(2), would perhaps obviate the need to seek such information in a complaint proceeding under section 3662, thus reducing the potential administrative burden on the Commission, the Postal Service, and third parties. In the absence of discovery rights, these Comments below contain suggestions regarding a number of areas where additional information should be sought from the Postal Service.

II. THE COMMISSION SHOULD ANALYZE THE ANNUAL COMPLIANCE REPORT AGAINST THE OBJECTIVES AND FACTORS OF PAEA.

A. Transition Issues

The Postal Service Annual Compliance Report explains that rates, fees, data collection, and reporting have been developed in a transitional phase between PRA and PAEA. *See* Postal Service Report, pp. 1-2. The Postal Service concludes on page 1 of the Report: "the 'applicable requirements of Title 39' that are relevant to the FY 2007 rates and fees are those of the PRA, not the PAEA." It is true that the postal rates in effect during FY 2007 were developed and implemented under PRA. Rates established in Docket No. R2005-1 were in effect from October 1, 2006 through May 14, 2007, and rates established in Docket No. R2006-1 were in effect from May 15, 2006 through September 30, 2007 (for all classes except

Periodicals, which rates did not increase until July 15, 2007).² However, the matter of applicable law is somewhat more complex than acknowledged by the Postal Service.

It is unfortunate that PAEA failed to provide guidance for a transitional compliance review by the Commission. The Commission is conducting the current review under PAEA, but PAEA does not specify that PRA or PAEA is the appropriate touchstone for the evaluation of rates. The Commission now must fill in this void in the statute. Certainly where PRA and PAEA contain the same requirements, such as the requirement that each class of mail cover its direct and indirect attributable and reasonably assignable costs, the Commission has maximum authority to make findings of noncompliance. *See, e.g.*, former 39 U.S.C. § 3622(b)(3) and current 39 U.S.C. § 3622(c)(2). Where the factors and objectives have changed, the matter is not so clear.

Further, the Commission's role in this transitional docket could and should play an important role in providing guidance to the Postal Service applicable to future rate increases, even though the next increase could be initiated before conclusion of this docket. *See* Order No. 43, p. 2, n. 3. To those ends, we discuss the Postal Service FY 2007 Annual Compliance Report for compliance with the Objectives and Factors of PAEA, and offer some observations for the future.

² Under PRA, the Commission's responsibility in a rate case was to issue a recommended decision to the Postal Service Board of Governors in compliance with PRA. The process was forward-looking to a future prospective test year. Under PAEA, however, the Commission's determination of compliance is an after-the-fact process of examining rates that were in effect during a prior fiscal year, and involves comparing those rates to the requirements and limitations of 39 U.S.C. Chapter 36. *See* 39 U.S.C. § 3563(b)(1).

B. PAEA Objectives**1. “To maximize incentives to reduce costs and increase efficiency” (39 U.S.C. § 3622(b)(1))**

This cost/efficiency objective can be interpreted as being pertinent to the entire rate structure. As one example, it obviously applies to workshare discounts, which encourage efficient use of resources. Any significant reduction in workshare discounts would be contrary to this objective.

This objective also can be applied to non-worksharing rate differentials. Prior to Docket No. R2006-1, Standard flats clearly were underpriced relative to letters. The disparity in contribution led to, and was used as justification for, the Bookspan Negotiated Service Agreement (“NSA”) (Docket No. MC2005-3), which gave one mailer a greater financial incentive to use letter-shaped mailpieces that make greater unit contributions. The Commission’s recommended decision in Docket No. R2006-1 led to rates which generally overcame this infirmity in the general tariff schedule.

Yet another example of failure to maximize incentives to reduce costs and increase efficiency is pricing of return services for First-Class presort letters. To this day, the Postal Service continues to provide First-Class presort letters that are undeliverable as addressed (“UAA”) (and cannot be forwarded) with free physical return, rather than charging presort First-Class mailers a fee for this expensive service. Reducing presort rates while levying an offsetting cost-based fee for physical return of First-Class presort letters would provide mailers with a meaningful incentive to reduce this cost. Mailers whose UAA mail is below average would gain, mailers with UAA mail equal to average would break even, and mailers with

above-average UAA mail would pay more.³ Such pricing also would convert UAA mail into a source of revenue, such as provided by other Postal Service special services.

This cost/efficiency objective is reinforced by factors 5, 7 and 12 (contained in § 3622(c)), which pertain, respectively, to (i) reducing costs, (ii) encouraging operational efficiency, and (iii) increasing efficiency and reducing costs. This objective is integral to rates and the rate process, and should be a subject of continuing discussion in annual compliance reviews.

2. “To create predictability and stability in rates” (39 U.S.C. § 3622(b)(2))

This objective obviously pertains to rates, and is properly included in any compliance review. Tension exists among this objective, and objective 1 (cost/efficiency), objective 4/factor 7 (“flexibility”) and 8 (“changes of unequal magnitude”). By itself, and with respect to the general tariff structure, this “double” objective of predictability and stability could be said to argue in favor of small, annual, near across-the-board percentage rate increases. To the extent that the Postal Service uses pricing flexibility (objective 4) and does in fact implement unequal rate increases (objective 8) within a class of mail in a manner designed to help maximize incentives to reduce costs and increase efficiency (objective 1), those mailers

³ In FY 2004, the most recent year available, 3.33 billion pieces of First-Class Mail were UAA — with nearly 64 percent of the UAA mail originating at presorted or automation pieces. Total cost to process UAA First-Class Mail, including the processing of address correction notices, was **\$1.03 billion**. See Docket No. PI2008-1, Public Representative Initial Comments in Response to Notice of Request for Comments on Service Performance Measurement Systems for Market-Dominant Products, pp. 10-11.

receiving above-average rate increases can urge that such “flexible” rate increases were not predicted, hence violate objective 2.

3. “To maintain high quality service standards established under section 3691” (39 U.S.C. § 3622(b)(3))

This objective speaks directly to (i) the service standards, which now have been promulgated, (ii) the performance measurement system, now under development, (iii) performance goals, which are to be submitted before June 20, 2008 and (iv) the Commission’s determination of compliance under section 3653(b)(2). Clearly, the Postal Service appears to be making a good-faith effort to comply with this objective. In general, any determination of compliance with this objective is premature. Nevertheless, some comments appear to be in order.

With respect to whether service performance met service standards, few data are available in this year’s Postal Service Report. However, among the limited service performance data now available are delivery confirmation data for parcels. According the Postal Service, only 57.7 percent of Package Service pieces with delivery confirmation received timely delivery in 2007. (Postal Service Report, p. 17.) Significantly, delivery confirmation records are the only data that the Postal Service indicates it intends to rely on for parcels. Thus, for Package Services, all available information can be boiled down to a single datum indicating the percent that met service performance standards. This is an interesting “dry run” for future reports. Clearly, 57.7 percent on-time delivery of parcels is not a satisfying result, as 42.3 percent of parcels with delivery confirmation did **not** meet service standards. Thus, it would be difficult to argue that the Postal Service complies fully with this

objective.⁴ The most disturbing aspect of this Report is that it appears that the Postal Service does not plan to provide any additional information on the 42.3 percent of parcels not achieving service standards, which often are referred to as “tail of the mail.” The Postal Service needs to provide additional information and focus more attention on the “tail of the mail” that did not receive timely delivery in order to assess compliance more fully. Without such information, it will be difficult, or perhaps impossible, to assess whether the Postal service is improving its compliance vis-a-vis this objective. Reporting on the **average number of days** late, as proposed in Valpak’s Initial Comments in Docket No. PI2008-1 (Jan. 18, 2008), would be a good start.

Once the performance system is in place, performance need not, and should not, be discussed in isolation from prior years. Year to year comparisons should be made. For example: Did **performance** in meeting service standards improve over last year? Or at least stay the same? Or deteriorate? Although perhaps not relevant this year for all products for which the Postal Service intends to measure performance, by next year the question posed here would be relevant for parcels (since we have a performance measure for parcels this year), and by the year after that it hopefully will be relevant for an expanding set of products.

Similarly, one can ask: Did **consistency** of service performance improve over last year? Or at least stay the same? Or deteriorate? Once data are available on the number of pieces that fail to meet a service standard, along with the extent to which they failed to meet

⁴ Although the Postal Service has not set any performance goals, it is hoped that no performance goal for meeting the pertinent service standard would be in the 55 to 60 percent range.

the service standard, consistency can be estimated in a variety of ways. Which way is “the best” way to measure consistency may be debatable, but for a start we have proposed a simple, straightforward statistic: “average days late” for all recorded pieces not delivered on time. The important point is that reporting on consistency needs to be viewed as integral to performance measurement, and at least one statistic on consistency needs to be provided. It is suggested that the Commission ask the Postal Service how it plans to report on consistency of service in its annual compliance reports.

Finally, another question that one could address in connection with this objective is: Did the Postal Service make adequate **progress** in measuring service performance? Although the law does not explicitly state that the Postal Service “has to make adequate progress,” it does lay on the Commission the responsibility of overseeing implementation of the law. The Postal Service never has had adequate performance data, but PAEA mandates that it develop such data. Although no time statutory frame is established, developing adequate data over a span of many years would not be responsive to the new law. This effort will be advanced by the Commission’s current work in Docket No. PI2008-1.

4. “To allow the Postal Service pricing flexibility” (39 U.S.C. § 3622(b)(4))

This objective clearly pertains to the ratesetting procedure and, inferentially, to rates set under PAEA, and relates to factor 7. As noted above under the discussion of objective 2 (“predictability and stability”), tension exists between that objective and pricing flexibility. However, since existing rates in FY 2007 were set under PRA, the Postal Service has not yet had an opportunity to exercise pricing flexibility. Only after the Postal Service has submitted

its first notice of rate adjustment under the new law can one comment on the extent to which rate changes reflect pricing flexibility.

Interestingly, “flexibility” is nowhere defined in the statute. It could be met by the speeding up of rate increases, which took about 12 months under PRA.

However, viewed another way, the Postal Service may be in the process of becoming locked into changing prices only once a year, at about the same general time each year, *e.g.*, May. If that should be the case, then with respect to the frequency and timing of rate changes, it appears that the Postal Service has not gained much flexibility, unless annual changes can be defined as “more flexible” than biennial or triennial changes which the Postal Service previously elected to utilize.

Under PAEA, the Postal Service has additional latitude with respect to setting individual rates within the cap for each class of mail, but the Commission appears to have a key role in the rate setting process which could be seen as supervisory, and sometimes reactive. This latitude is perhaps the “pricing flexibility” that was intended, and now is allowed to the Postal Service. Should this interpretation be correct, the “data” pertinent to the compliance review would need to inform the Commission as to why the Postal Service has deviated from an across-the-board percentage rate change.

5. “To assure adequate revenues, including retained earnings, to maintain financial stability” (39 U.S.C. § 3622(b)(5)).

The timing and amount of rate changes directly affect revenues, hence compliance with this “adequate revenues” objective clearly needs to be addressed. This objective can be evaluated with data from the CRA for FY 2007 (attachment No. USPS-FY07-1 to the Postal

Service FY 2007 Annual Compliance Report), with the caveat that the FY 2007 CRA reflects rates from both Docket No. R2005-1 and Docket No. R2006-1. Although none of the rates in effect during FY 2007 were set under PAEA, it is noted that the necessity of having to evaluate compliance with this objective using data from two rate regimes during the prior fiscal years seems likely to be a recurring problem. That is, assuming the Postal Service elects to file for an annual rate increase every May, then one set of rates will be in effect for, approximately, the first six months of each fiscal year, and a second set of rates will be in effect for the remaining six months.⁵

The FY 2007 CRA (PRC Version), USPS-FY07-1, shows the following summary result (in millions):

Total revenue (incl. investment income)	\$ 74,972.8
Less: Total operating expenses	<u>-77,156.8</u>
Net operating profit (deficit)	(2,184.0)
Escrow funding reconciliation	<u>- 2,958.4</u>
Total profit (deficit)	(\$ 5,142.4)

Thus, according to the FY 2007 CRA, operating revenues were \$74,972.8 million, and operating costs were \$77,156.8 million, resulting in an **operating deficit** of some \$2,184.0 million, **before** the Escrow Funding Reconciliation (which increased the FY 2007 deficit to \$5,142.4 million).⁶ Funding of Retired Employee Health Benefits ends after 10 years. This **operating** deficit indicates that in FY 2007 the Postal Service was not in a long-run sustainable

⁵ Each annual compliance report will contain costs for the prior fiscal year, but those costs will have to be compared with revenues from two different sets of rates.

⁶ This deficit shows up on the Postal Service's balance sheet as a reduction in capital. At the end of FY 2006, total net capital was \$6,276 billion, and at the end of FY 2007, total net capital was \$1,134 billion, a reduction of \$5,142 billion.

financial “equilibrium.” It incurred an operating deficit which, if continued at this rate, ultimately will cumulate and be a contingent liability of the federal government. Although Congressional intent regarding PAEA may not be altogether clear, it seems reasonable to infer that such a result is not among the ends that Congress (or the Government Accountability Office (“GAO”), or the Department of the Treasury) intended PAEA to accomplish. That deficit, of course, is why an omnibus rate increase under PRA was implemented in May 2006. Whether rates currently in effect are adequate to cover costs is not known. The net operating deficit of \$2,184 million represented a revenue shortfall of 2.9 percent, and the total deficit of \$5,142 million represented a revenue shortfall of 6.9 percent. Since the Docket No. R2006-1 rate increase was estimated to increase rates, on average, by 7.6 percent, and generate almost \$4 billion of additional revenue,⁷ current revenues may in fact be covering costs.⁸

6. “To reduce the administrative burden and increase the transparency of the ratemaking process” (39 U.S.C. § 3622(b)(6))

Although directly pertinent to the ratemaking process, this two-part objective is not capable of evaluation at this time. On the basis of regulations which the Commission has promulgated to date, however, it would appear that administrative burden accompanying rate increases and the entire rate cycle, including the annual compliance review, will be somewhat

⁷ Docket No. R2006-1, *Op. & Rec. Dec.*, Vol. 1, p. i.

⁸ As indicated here, total FY 2007 operating expenses amounted to \$77,156.8 million. In Docket No. R2006-1, total accrued costs for the Test Year, FY 2008, were estimated by the Commission at \$76,788.8 million. *Op. & Rec. Dec.*, Appendix C. FY 2007 actual operating costs thus exceeded FY 2008 projected operating costs by 0.5 percent. It remains to be seen whether a rate increase equal to the Consumer Price Index (“CPI”) cap, implemented in May of 2008, will provide revenues sufficient to cover FY 2008 operating costs.

reduced. In particular, the need to roll base year revenues and expenses forward to a prospective test year no longer exists. Nor does the Postal Service need to estimate and defend a contingency, or otherwise prepare extensive testimony to accompany its request for higher rates.

With respect to data (or other information) that would bear on this objective, the cost of rate case preparation was never broken out separately in Postal Service data, nor does the extant filing contain any data pertinent to this objective. Consequently, it seems likely that assessment of compliance with the first part of this objective always will be qualitative.

Whether transparency under the new ratemaking process has been (or will be) increased is another question, and is not known at this time, but largely will be determined by future regulations the Commission issues detailing information to be filed by the Postal Service in its annual compliance report.

7. “To enhance mail security and deter terrorism” (39 U.S.C. § 3622(b)(7))

It is difficult to see how the ratesetting procedure, rates charged, or service provided pertain to this objective. Furthermore, it is difficult to see what general data or other routine information would pertain to this objective.

One might opine that introduction of the Intelligent Mail Barcode (“IMB”) will somehow help enhance mail security, but upon reflection any such position appears to be a stretch. To the extent that it is relevant, though, certain possible connection is noted between this objective and factor 13, which states the need to consider “[t]he value to the Postal Service and postal users of promoting intelligent mail and of secure, sender-identified mail.”

8. **“To establish and maintain a just and reasonable schedule for rates and classifications, however the objective under this paragraph shall not be construed to prohibit the Postal Service from making changes of unequal magnitude within, between or among classes of mail” (39 U.S.C. § 3622(b)(8))**

“Just and reasonable,” like beauty, often exists only in the eye of the beholder. The tension that exists between this objective and objective 2 (“predictability and stability”) is discussed *supra*. It is not clear how one could design an objective test to determine that rates set under the new law violated this standard. However, rates which ignore costs known to be accurate and demand factors could qualify. The explicit authorization to make “changes of unequal magnitude within, between or among classes of mail” seemingly guarantees the Postal Service a measure of flexibility in rate setting.

9. **“To allocate the total institutional costs of the Postal Service appropriately between market dominant and competitive products” (39 U.S.C. § 3622(b)(9))**

This exercise was not carried out under the PRA, and no cost data submitted with the FY 2007 Annual Compliance Report make any allocation of institutional costs. However, a procedure for determining an appropriate allocation of institutional costs is being developed by the Commission. *See* 39 U.S.C. § 2011(h)(2), and Docket No. PI2008-2, Review of Treasury Report, Commission Order No. 56, Notice and Order Providing an Opportunity for Comment on Treasury Report.

C. PAEA Factors

1. **“The value of the mail service actually provided each class or type of mail service to both the sender and the recipient, including but not limited to the collection, mode of transportation, and priority of delivery” (39 U.S.C. § 3622(c)(1))**

Under PRA, this factor generally was based on the nominal service standards specified for each class of mail, and never on service **actually** provided. The nominal service standards often were referred to as “intrinsic value.” Consequently, application of this factor was in no way “data-based.” It was limited to generalities, such as (i) Express Mail receives better service than Priority Mail, hence has more value; (ii) Standard Mail is not entitled to air transportation, and is deferrable and processed after First-Class Mail, hence it has less value; etc.

Under the new law, performance data are supposed to be provided for products in each class of mail. When such performance data become available, it then may be possible to examine the data and look at the service “actually provided” to different products and classes of mail, *i.e.*, interpret the wording of the statute literally, as written. For now, of course, no performance data are available, so this factor cannot be applied to the FY 2007 Annual Compliance Report.

2. **“The requirement that each class of mail or type of mail service bear the direct and indirect postal costs attributable to each class or type of mail service *through reliably identified casual relationships* plus that portion of all other costs of the Postal Service reasonably assignable to such class or type” (39 U.S.C. § 3622(c)(2) (emphasis added))**

As indicated previously, this factor was the only “requirement” under PRA. However, despite being a requirement, the Periodicals class failed to cover its attributable costs as measured over a period of many years. Requiring each class of mail to cover its attributable costs is a proscription against cross-subsidy between the various classes of mail.

The FY 2007 CRA (USPS-FY07-1) provides revenues and attributable costs for each class of mail, and those data reveal that Periodicals again failed to cover their attributable costs. Revenues were \$2,187.9 million, attributable costs were \$2,635.6 million, the shortfall was \$447.7 million, and coverage was only 83.01 percent. Thus, Periodicals did not cover their attributable costs, as required by PRA (which was in effect when the rates in effect during FY 2007 were set) and also as required by factor 2 of PAEA. *See* Section V, *infra*.

PAEA has replaced the prospective test year, which inevitably incorporated a number of assumptions, with after-the-fact accountability (which did not exist under the PRA), via the annual compliance review.⁹ Such after-the-fact accountability does not bode well for Periodicals, where unrealistic “cost reduction” assumptions have been used in the roll-forward model in rate case after rate case to justify rates that consistently failed to cover attributable costs. Review of this factor surely should be an integral part of the annual compliance review.

⁹ United Parcel Service (“UPS”) did file a complaint case once saying parcels were below cost, after the fact.

3. “The effect of rate increases upon the general public, business mail users, and enterprises in the private sector of the economy engaged in the delivery of mail matter other than letters” (39 U.S.C. § 3622(c)(3))

In rate cases under PRA, the first step was to establish the revenue requirement, which then governed the average rate increase. One use of this factor, by both the Postal Service and the Commission, was to justify tempering rate increases for individual high-cost rate categories. Such tempering, continued in rate case after rate case, with no intermediate attempt to “true up” markups, ultimately led to situations like that which surfaced in the Bookspan NSA (Docket No. MC2005-3), where the markup on flats was so low that the Postal Service was willing to pay Bookspan to convert its flats to letter-shape mail. This problem was addressed by the Commission in Docket No. R2006-1.

At the other extreme, this factor, in conjunction with factor 4, *infra*, also was used to restrain prices from being “too low” vis-a-vis competitors “engaged in the delivery of mail matter other than letters” — *e.g.*, UPS, FedEx, newspapers (inserts), and private distributors of advertising material.

It should be noted that this factor, if given an interpretation under PAEA similar to that under PRA — *i.e.*, to skew markups and keep rate changes closer to the average than they otherwise might be — would be somewhat counter to the provision in objective 8, which explicitly says that the Postal Service shall **not** be prohibited “from making changes of unequal magnitude within, between or among classes of mail.”

Skewing of markups for non-economic reasons, as occurred in prior rate cases, is counter to making (or maximizing) a profit. For example, within the Periodicals class, the

restrained markup on, and rate for, small high-cost publications is what causes failure of the class as a whole to cover attributable costs. With respect to the annual compliance review, one could attempt to ascertain whether the Postal Service puts too much emphasis on this factor.

4. “The available alternative means of sending and receiving letters and other mail matter at reasonable costs” (39 U.S.C. § 3622(c)(4))

Previously, this factor was applied to what PAEA now refers to as “competitive products.” It generally was used to set a floor under rates for competitive products, so that the Postal Service could not be accused of subsidizing or competing unfairly. This factor may be redundant with the various provisions of PAEA that pertain to competitive products, *e.g.*, provisions that require (i) a fair allocation of overhead to competitive products, (ii) revenue from competitive products collectively to cover incremental costs, (iii) any profit on competitive products to be “taxed,” etc. Collectively, those provisions virtually guarantee that rates for competitive products will conform with this factor.

5. “The degree of preparation of mail for delivery into the postal system performed by the mailer and its effect upon reducing costs to the Postal Service” (39 U.S.C. § 3622(c)(5))

This factor is consistent with objective 1. In prior rate cases, its predecessor 39 U.S.C. § 3622(b)(3) has been used to support workshare discounts, which have increased gradually to the point where they generally represent 100 percent of costs avoided. Objective 1 can be seen as even stronger than former 39 U.S.C. § 3622(b)(3) since it now specifies “maximize incentives.” The annual compliance review thus should focus attention on objective 1.

6. “Simplicity of structure for the entire schedule and simple, identifiable relationships between the rates or fees charged the various classes of mail for postal services” (39 U.S.C. § 3622(c)(6))

Application of this factor has been largely to mail products used by the general public. Both the Postal Service and the Commission have favored restraint and gradualism when it came to complicating changes in the rate structure for products used by the general public. Nevertheless, and despite the existence of this factor, over time the rate structure for First-Class Mail has undergone a gradual evolution that has added to complexity. For instance, a rate decrement for additional ounces in excess of the first ounce has become a fixture, along with surcharges for square envelopes (or other envelopes that fail the aspect ratio test). In Docket No. R2006-1, the Postal Service further increased complexity by introducing shape-based pricing for First-Class single piece letters and flats.

This factor has not constrained the complexity of rates for bulk categories, such as presort First-Class Mail, Periodicals, or Standard Mail, nor has it been perceived as being applicable to categories of mail entered by more sophisticated mailers.

7. “The importance of pricing flexibility to encourage increased mail volume and operational efficiency” (39 U.S.C. § 3622(c)(7))

This factor did not appear in PRA, hence it has no prior history comparable to other factors. This factor also is consistent with, and reinforces, objective 1 (costs/effeciency). *See* discussion under objective 4 (“pricing flexibility”), *supra*.

- 8. “The relative value to the people of the kinds of mail matter entered into the postal system and the desirability and justification for special classifications and services of mail” (39 U.S.C. § 3622(c)(8))**

This factor relates more to classifications than to rate setting, but its predecessor has been used to support the finding that the Postal Service could establish niche classifications and enter into NSAs under PRA. It is not altogether clear how one would assess compliance with this factor in an annual compliance review. *See* Section II.C.10, *infra*.

- 9. “The importance of providing classifications with extremely high degrees of reliability and speed of delivery and of providing those that do not require high degrees of reliability an speed of delivery” (39 U.S.C. § 3622(c)(9))**

This factor also relates more to classifications than to rate setting. Absent any classification change during the prior year, it is not altogether clear how one would assess compliance with this factor in an annual compliance review.

- 10. “The desirability of special classifications for both postal users and the Postal Service in accordance with the policies of this title, including agreements between the Postal Service and postal users, when available on public and reasonable terms to similarly situated mailers, that—**
- (A) either—**
 - (i) improve the net financial position of the Postal Service through reducing Postal Service costs or increasing the overall contribution to the institutional costs of the Postal Service; or**
 - (ii) enhance the performance of mail preparation, processing, transportation, or other functions; and**
 - (B) do not cause unreasonable harm to the marketplace” (39 U.S.C. § 3622(c)(10))**

This factor is new, and seems aimed at removing any doubt about legitimacy of niche classifications (*e.g.*, Weight-Averaged Nonletter-Size Business Reply Mail, Docket No. MC99-2) and NSAs. In order to evaluate whether NSAs in force during the prior fiscal year

actually comply with the above-stated provisions, the Postal Service would need to submit financial and other performance data on outstanding NSAs. No such data are included in the FY 2007 Annual Compliance Report. If the justification for an NSA were purely “enhanced performance,” evidence about increased performance seemingly should be submitted.

11. “The educational, cultural, scientific, and informational value to the recipient of mail matter” (39 U.S.C. § 3622(c)(11))

This factor has been used to justify a low markup on certain classes, especially periodicals, but also Bound Printed Matter (“BPM”) and Media Mail.

12. “The need for the Postal Service to increase its efficiency and reduce its costs, including infrastructure costs, to help maintain high quality, affordable postal services” (39 U.S.C. § 3622(c)(12))

This factor is consistent with, and reinforces, objective 1 (rates/efficiency). One certainly could inquire as to whether the Postal Service has availed itself of obvious improvements to the general tariff structure. For instance, as noted under the discussion of objective 1, Postal Service executives often note the high cost of returning UAA First-Class Mail, yet the Postal Service never implements a fee for physical return of such mail. Such repeated failure to modify the tariff structure in ways that would encourage mailers to increase efficiency and reduce costs could be an obvious subject for comment as part of an annual compliance review.

13. “The value to the Postal Service and postal users of promoting intelligent mail and of secure, sender-identified mail” (39 U.S.C. § 3622(c)(13))

Starting in January 2009, the Postal Service plans to require use of the Intelligent Mail Barcode as a prerequisite for bulk mail to obtain barcode and presort discounts. Other than

noting the advent of this new requirement, it is not altogether clear how one would assess compliance with this factor in an annual compliance review.

14. “The policies of this title as well as such other factors as the Commission determines appropriate” (39 U.S.C. § 3622(c)(14))

This is a catchall provision for the Commission’s judgment, but obviously would be difficult to address in the abstract.

III. THE POSTAL SERVICE REPORT REVEALS ANOMALIES IN CERTAIN STANDARD MAIL COSTS THAT MAKE THEM UNRELIABLE FOR RATEMAKING.

The significance of the cost of mail products has not disappeared with passage of PAEA. Indeed, the requirement that classes cover their costs (§ 3622(c)(2)) coupled with requirements for adequate revenues and retained earnings (§ 3622(b)(5)), as well as increased transparency (§ 3622(b)(6)), calls for accurate, reliable, and generally better cost data. *See generally* Docket No. RM2007-1, Valpak Reply Comments on Order No. 26 (Oct. 9, 2007), p. 29-34.

A. General Principles Applicable to the Relationship between Rates and Costs under PAEA

PAEA alters the PRA framework for setting rates, and supplies guidance for decision making within the new framework. The scheme is clear. Rates no longer are to be set to achieve an **overall breakeven** — *i.e.*, where total revenues equal total costs. Instead, a constraint on the average level of rate increases, in the form of an upper limit, is provided by a price cap, which reflects changes in the CPI. With the disappearance of a breakeven requirement, the linkage between total revenues and total costs is said to be broken. Of

course, an important tie between total revenues and total costs continues to lurk in the background, and would become manifest if the Postal Service were to file an exigent rate case to obtain rates above the cap in order to cover costs.

Abolishing the long-established link between total revenues and total costs does not mean that costs should no longer play an important role in ratesetting under PAEA. Quite the contrary. Because financial breakeven is no longer guaranteed by the new law, now, more than ever, the Postal Service must strive for accurate, reliable product costs. The following describes the relationship between costs and rates under PAEA.

To begin, PAEA specifies that the cap is to be applied to each **class** of mail individually. This means that no considerations of national policy, or of any other kind, can empower the Postal Service to increase rates in one or more classes **less than** the cap, and in one or more classes correspondingly **more than** the cap. The arguments for the framework that has been established are understood to be threefold.

First, the constraint on rates, coupled with incentives to increase net income, puts pressure on the Postal Service to introduce **new products** (of value to mailers) that make a positive contribution.

Second, the desire to increase net income provides an incentive for the Postal Service to **reduce its costs** in beneficial ways, possibly through technological innovation.¹⁰

¹⁰ Lower costs *per se*, of course, are not inherently desirable, because they could be achieved in undesirable ways, such as by artificial limitations on volume, lowering service levels, or eliminating entire categories of mail (such as classes or subclasses).

Third, a firm operating under a price cap has incentives that, if acted upon, will tend to move it toward rates that are more **economically efficient**, thereby bringing about increases in welfare.

The importance and desirability of all three of these outcomes is emphasized repeatedly by the new law. Specifically:

- 1) A new separate **subchapter III** is provided to guide the development and introduction of new products.
- 2) **Section 3622(b)(1)** requires that the ratesetting system shall be designed “[t]o maximize incentives to **reduce costs** and increase efficiency.” Rates can encourage the efficiency of the postal sector in two ways:
 - a) setting rates that are economically efficient can lead to welfare increases for some mailers that are larger than welfare losses of other mailers; and
 - b) rates can be set to induce mailer responses that increase efficiency, such as when a mailer spends \$100 to change its mail preparation in a way that allows the Postal Service to save, say, \$400.

Also, **Section 3622(c)(12)** refers to increasing efficiency and reducing costs.

The emphasis on setting rates to increase efficiency is new in PAEA, as PRA did not contain corresponding guidance. The focus on net income gives the Postal Service added incentive to avoid volume that is carried below cost. In fact, losing all such volume would make the Postal Service better off, rather than worse off.

- 3) **Section 3622(b)(8)** calls for “just and reasonable” rates. In the private sector, competition generally is viewed as bringing about rates that are just and that bear a reasonable relationship to costs, thereby increasing economic welfare. The new law requires that rates do likewise in the postal sector.
- 4) **Section 3622(c)(1)** requires attention to the “value of the mail service,” which is precisely the focus of notions of economic efficiency and public interest pricing. Setting prices to realize revenue from mail that is valued highly, instead of from mail that has little excess value to sustain it, promotes welfare.
- 5) **Section 3622(c)(3)** requires attention to the “effect of rate increases” on the nation and mailers.¹¹ This factor might be read to caution against overly large rate changes. At the same time, no increases in economic efficiency or welfare can be realized without effects on mailers. When rates are changed, appropriate incentives must be provided, effects must exist, and mailers must adapt. To suggest otherwise is to argue for preservation of the status quo. In addition, **section 3622(b)(8)** provides a specific reminder that an interest in “just and reasonable” rates should not be interpreted to ward off price changes of “unequal magnitude.”
- 6) **Section 3622(c)(7)** points to the “importance of pricing flexibility to encourage increased mail volume and operational efficiency.” This points to the inefficiency of placing rate burdens on mail with little surplus value, which

¹¹ Since rate “increases” can be negative (rate decreases), section 3622(c)(3) can be viewed as requiring attention to the effect of rate “changes” on the nation and mailers.

would unduly lower volumes. The intent, then, goes clearly to the kind of economic efficiency discussed above.

Focusing attention on these aspects of PAEA requires attention to accurate costs as well as market considerations, regardless of how rates are derived. However, instead of reviewing rates before they are implemented, the task in a compliance review (after this year) will be to review under PAEA rates set previously under PRA by the Postal Service.

It should be noted that the importance of accurate costs is relative to the guidance they should provide to what happens among products within classes. An emphasis on markets and economic efficiency, which requires attention to elasticities and other factors, does not argue for reduced emphasis on costs. Indeed, all notions of competition, profitability, and economic efficiency rely heavily on having available accurate and reliable cost information. In the often-referenced Ramsey formulas, for example, the role and importance of the cost variables are just as clear and just as strong as those of the elasticity variables.

Of course, under PRA, the Commission has emphasized accurate costs strongly in all of its ratesetting activities, particularly in regard to intra-class rate relationships. And although information available on markets has been sometimes limited, markets have not been ignored. Had more information relating to demand relationships been available, undoubtedly it would have been considered.

In conclusion, notions of cost and demand are important under both the old and the new law. Moreover, without good information on costs and demand, rates cannot be assessed against the PAEA criteria discussed above, in a compliance review or in any other place, either on an *ex post* or *ex ante* basis. If market considerations are to receive greater attention under

the new law, as seems to be suggested by PAEA itself and by commenting parties, an associated analytical burden then falls on the Postal Service, because, as noted above, available information on markets has left much to be desired. Thus, in this review, little can be said about markets or market considerations. On the subject of costs, however, considerable information has been made available.

B. Type of Costs Needed for Annual Compliance Review

Before discussing the costs that have been submitted in the instant docket, it is helpful to step back and consider the nature of the cost information needed. Obviously, costs should measure actual Postal Service operations to a sufficient degree that they are capable of reliably determining (or at least reliably estimating) the cost associated with any rate being assessed. Costs for any year, including FY 2007, may not be satisfactory for any number of reasons.

For example:

- 1) Costs could be **out of date** in terms of wage levels and other factor prices. This issue does not pertain, however, to costs presented in this review, as discussed *infra*.
- 2) Costs could relate to **volumes** that are inconsistent with the rates being reviewed. Except for Periodicals, whose rates changed on July 15, 2007, all rates under review in this docket were implemented on May 15, 2007. If mailing patterns changed after this date due to the new and different mix of rates, as would be expected, then volumes for the year and the associated costs may not be reflective of the rates being reviewed. Adjusting for this problem is

difficult. It appears that this problem will infect all future annual compliance reviews.

- 3) The Postal Service could have changed the way it **processes** the mail, and costing models used in the past could have out-of-date mail flows, productivity levels, or piggyback factors. Such factors change regularly, and the Postal Service should make adjustments accordingly. Some of the costs presented in this docket have been adjusted for these kinds of changes.
- 4) In mid-year, a **mailing requirement** could have been changed. An example of this occurring is the implementation of a requirement that basic carrier-route letters in ECR be automation-compatible. Similarly, a category could be eliminated, as has occurred for basic automation letters in ECR. Adjustments for these kinds of changes are more difficult to make, and it is not clear that they have been made in this case.

Under PRA rate cases, the Postal Service presented cost information through sworn testimony. Interested parties could analyze cost materials and file discovery. After a record was developed using the adversarial process, final costing decisions were made by the Commission as an independent expert body. A great deal about costs was learned through this on-the-record process. Outside experts with various areas of expertise were engaged by mailers, the Office of the Consumer Advocate (“OCA”), and the Commission. Many of those experts had considerable costing experience over a range of industries; they provided testimony and made suggestions, all of which was made available at no cost to the Postal Service. During this process, errors were uncovered, improvements were made, and suggestions were

made for future consideration. Many of the benefits from this process are at risk of being lost under PAEA.

On an ongoing basis, the Postal Service and its contractors manage a considerable range of costing systems and perform a number of special cost studies. Many of the people involved, such as statisticians and systems engineers, work full-time on specific systems, such as the Revenue, Pieces, and Weight (“RPW”) system. They visit facilities, work with operating people, learn to evaluate results, identify anomalies, and make improvements in their systems. Hopefully, in the PAEA environment, these people will continue to work to improve costing — though the opportunity mailers have had to question and challenge their findings has been curtailed.

In fact, under PAEA, the Postal Service should have more interest than before in developing accurate costs. No firm can be competitive and watch out for its own interests if it does not have good information on its costs. Accordingly, and in view of the attention given to accurate costing in PAEA, discussed *supra*, the Postal Service should have more incentive than ever to develop costs that are reliable and replicable.

But even with all the proper incentives, it is possible for costing systems to generate costs that are anomalous, counter-intuitive, unreliable, and not sufficient for rate setting, as illustrated in section III.C, *infra*. Certain costs presented for FY 2007 fluctuate in surprising degree from costs accepted by the Commission in Docket No. R2006-1. It can be expected that Postal Service pricing personnel will look for and not rely on aberrant costs. However, the Commission’s regulations governing the annual compliance review should establish a way for mailers to inquire into, and even challenge, such results. A compliance review that must

rely on defective costs cannot reach meaningful conclusions. And, if the source of the costing anomalies cannot be identified, mailers are at risk that (i) the Postal Service could use these aberrational costs for ratesetting purposes, and (ii) after a rate increase is filed, their opportunity to question those rates will be severely limited.

C. Costs in this Annual Compliance Review

1. Changes in Costing under PAEA

In the instant docket, the Postal Service has presented costs that involve numerous and substantial changes from those relied on by the Commission in Docket No. R2006-1.

First, costs in Docket No. R2006-1, on which current rates are based, were FY 2005 costs rolled forward to FY 2008, while costs provided in the instant docket are actual FY 2007 costs. One could hypothesize that the roll-forward process is reasonably systematic and is dominated by inflation. If this were the case and the inflation level were about 3 percent per year, the expectation might be that the FY 2007 costs under review would all be approximately 3 percent below the projected FY 2008 costs on which current rates are based. Actual results, however, differ by far more than this.

The costs provided by the Postal Service in this docket have been updated in many regards, such as reflecting current wage levels and current prices for materials. They reflect current data collected by such systems as the In-Office Cost System (“IOCS”).¹² They reflect

¹² The aberrational ECR mail processing costs discussed *infra* could indicate that it may be time for a complete re-examination of the applicability of a workplace sampling system in a day and age when mailpieces no longer are worked individually by hand, as they were when the IOCS was developed. Automation, now in the form of Flats Sequencing System (“FSS”) deployment, continues apace. The time finally may have come when the Postal Service should completely re-examine the utility of the IOCS, rather than continuing to patch it

volume levels for the FY 2007 year (though these volumes may not relate well to the current rates that went into effect about five-eighths of the way through the year). Also, they contain numerous adjustments to accord with the current operating environment, as explained in USPS-FY07-2 and USPS-FY07-31.¹³

However, the Postal Service's Report is completely devoid of any **testimony or discussion** of the costing results presented. PAEA requires the Postal Service annual report to “**analyze** costs, revenues, rates, and quality of service.” 39 U.S.C. § 3652(a)(1). No comparisons are made with previous costs; no explanations are provided for costs that appear out of line; and no information is provided on changes in operations. There is no explanation of why current rates are appropriate — which is the central issue before the Commission under the new law. Previously, testimony, coupled with an opportunity for mailers to ask questions on these matters, provided transparency that now is missing, at least until the Commission issues regulations governing the annual compliance review.

Testimony on matter such as those discussed above can be quite valuable, since the Postal Service employs costing and ratemaking professionals, including contractors, who focus on these issues. It is their job to maintain an understanding of relevant markets. Without such discussion in testimony under PRA, mailers and the Commission are largely on their own to analyze a vast body of information containing numerous undocumented changes.

up in an effort to accord with a changing environment that increasingly makes it obsolete.

¹³ With respect to Periodicals, more detailed adjustments were made in the Periodicals cost model, which has required two technical conferences. *See* USPS-FY07-11.

2. ECR Costs

Based on available information, and in the limited time available, Valpak has been able to perform only a limited review of the primary costs — specifically the **mail processing** and the **carrier** costs — that underlie rate differences among rate categories in ECR.¹⁴ In Docket No. R2006-1, these two categories of costs constituted 90.85 percent of all costs allocated to ECR. *See* USPS-LR-L-135. Even if the Postal Service focuses the next rate adjustment on the new (mixed) product of saturation and high-density letters together, among other products now in ECR, these two categories of costs would remain central. Several observations concerning anomalous ECR costs can be made:

- 1) Looking at mail processing and carrier costs together,
 - the cost of **saturation letters** has increased 16.3 percent, while
 - the cost of **basic letters** has increased 23.3 percent.¹⁵
 (Presumably, these costs are unaffected by results for the low-volume category of high-density letters, which decreased 7.3 percent.)

- 2) Still looking at mail processing and carrier costs together,
 - the cost of **saturation flats** has *declined* 2.0 percent, while
 - the cost of **basic flats** has increased 9.6 percent.
 (Presumably, these costs are unaffected by results for the low-volume category of high-density flats, which increased 12.3 percent.)

- 3) The costs for **ECR parcels** have behaved far more erratically, with
 - **high-density parcels** increasing a whopping 1,700.3 percent, and
 - the cost of **saturation parcels** up 67.7 percent, to 70.0 cents per piece.
 Since saturation parcels would receive virtually no mail processing (a cost shown to be 1.3 cents) and would be carried as an additional bundle on the

¹⁴ The costs shown are provided in USPS-FY07-18 and USPS-FY07-19.

¹⁵ As explained above, these (and all increases discussed in this section) are increases in FY 2007 costs as reported in the instant docket relative the costs on which the current rates were set in Docket No. R2006-1, which were projections for FY 2008.

street, requiring the carrier to do little more than reach into a container and put one in each mail box, it would seem difficult to explain a cost this high.

4) The carrier cost for

- **saturation letters** is shown to be 3.708 cents, while
- **saturation flats** is shown to be 3.749 cents.

Rounded to the nearest tenth of a cent, which is all that is recognized in ratemaking, the costs for these two very different items, very surprisingly, are now reported to be the same. To the extent to which saturation letters are delivery point sequenced (“DPS’d”), there should be virtually no in-office cost (an in-office cost for city carriers of 0.79 cents is shown, which is rather small) and letters on the street should be delivered with the full batch of letters for each stop, which should lead to a very low carrier cost, consistent with all the mail processing costs that are incurred for work being done by the DPS machine. These results are counter-intuitive.

5) If one looks at the **street** cost only for **city** routes,

- **saturation letters** show 1.64 cents, and
- **saturation flats**, which always require individual handling, show 1.55 cents.

These results also are counter-intuitive and also suspect in view of the much heralded efficiencies of the DPS program.¹⁶

These anomalous costs are not useful either for the present compliance evaluation, or for use in setting rates in the future. One certainly could not view it as fair for mailers to see rate increases based on changes in costs which cannot be explained, and are often anomalous and counter-intuitive.

When outcomes cannot be unexplained, as it appears these cannot be, several options are available. One is to raise fundamental questions about the costing techniques in use. For example, it is not clear that the statistical techniques of econometrics are really capable of

¹⁶ See 2007 Comprehensive Statement on Postal Operations, p. 44 (“DPS reduces costs, improves accuracy and speed of delivery, and contributes to improved customer satisfaction.”); Postal Service Strategic Transformation Plan 2006-2010, September 2005, p. 27 (“The Postal Service has had success controlling rising delivery expenses through automation efforts such as delivery point sequencing for letters.”).

allowing street costs to be inferred, at least not with the current data set. Another is simply to reject the result. For example, it is accepted that a demand analysis yielding a positive coefficient for price should be rejected and the investigator sent back to the drawing board. Similarly, a result that is higher or lower than any logic would suggest it should be, particularly relative to other results (as appears to be the case for the city street costs of saturation letters) should be rejected. Finally, it is possible to override a result. That is, if an understanding of the operating system argues persuasively that result B should be between result A and result C, and it is not, business could proceed as though the result were some intuitive proportion of the way between the two.

D. ECR Cost Coverage, Marketing Factors, and Elasticity

Under PAEA, a broader perspective can be taken in regard to saturation letters. As explained *supra*, the Postal Service is expected to give greater consideration to marketing factors in ratesetting. This means that accurate costs continue to be the starting point, after which there is markup. Saturation letters and their small-volume cousin, high-density letters, together, are considered in the proposed Mail Classification Schedule to be a separate and distinct product. This raises the question of the appropriate markup for this product. Currently, its markup is very high. As explained below, this outcome would not occur if rates were economically efficient.

It is widely believed that the own-price elasticity of saturation letters is among the highest of any mail product, and that its high elasticity has been a principal driver of the high elasticity that has tended to be found for the ECR subclass as a whole. It appears, however, that the specific level of this elasticity is unknown to the Postal Service. Nevertheless, if,

under PAEA, the Postal Service is focused on net income and prices are set to bring about economic efficiency in accordance with the objectives and factors in PAEA, it needs either to know this elasticity or to price on a best guess, a practice not uncommon in private firms faced with risky or difficult-to-analyze situations. The broader perspective, then, could be to lower the markup on saturation letters, possibly while recognizing that questions about its costs and elasticity exist.

The cost coverage shown for ECR in FY 2007 in the file FY07CRA.xls, in USPS-FY07-1, is **189.5 percent**, which includes ECR Nonprofit at its lower rate. If the new, higher rates had been in effect all year, coverage probably would be in neighborhood of **195 percent**. In his Statement before the Subcommittee on Federal Workforce, Postal Service, and the District of Columbia, Committee on Oversight and Government Reform, U.S. House of Representatives, on October 30, 2007, James C. Miller III, Chairman of the Board of Governors of the U.S. Postal Service, discussed efficient rates and the recognition of marketing and other factors, and pointed to a cost coverage for ECR of **104 percent** as being optimal to “maximize economic efficiency” (p. 1, Table 3). <http://federalworkforce.oversight.house.gov/documents/20071030122312.pdf>. Since cost passthroughs between the major categories in ECR in Docket No. R2006-1 approximated 100 percent, the current cost coverage on the new high-density and saturation letter product, would be expected to be notably above the coverage for ECR, and thus quite far from the economically efficient level.

IV. THE BILLING DETERMINANTS GENERATE QUESTIONS ABOUT DETACHED ADDRESSED LABELS AND MIXED LETTERS.

A. The Billing Determinants raise unanswered questions about the number of DALs, which the Commission should address to the Postal Service

Most of the data presented in the Billing Determinants are familiar from repeated, annual presentation, and are reasonably understandable without further elaboration. Occasionally, however, fundamental changes occur with data recorded in and made available only via the Billing Determinants, and transparency necessitates explanation, because the new data do not speak for themselves. Such a change is presented in the FY 2007 Billing Determinants, where the ECR flats page indicates 528,936,416 detached address labels (“DALs”).¹⁷

As background, prior to FY 2007, billions of DALs were mailed annually, but the Postal Service neither levied a separate charge on, nor collected any data concerning, the volume of DALs that were entered. The Postal Service simply recorded the volume of flats entered, and made no effort to distinguish between those unaddressed “wraps” that were accompanied by DALs and those bound, addressed flats (“catalogs”) mailed without DALs. In Docket No. R2005-1, the Postal Service provided an estimate of the number of DALs in the system, which was revised after discovery and testimony by Valpak. *See* Docket No. R2005-1, *Op. & Rec. Dec.*, ¶¶ 6078-80.

However, the Postal Service indicated that it had underway plans to collect data on the volume of DALs. *See* Docket No. R2005-1, *Rebuttal Testimony of Postal Service Witness*

¹⁷ USPS-FY07-4.

James M. Kiefer, USPS-RT-1, p. 31-32. The Commission now has before it the 528.9 million volume indicated above. But this datum, standing alone, raises questions. For instance:

- Do all DALs recorded in the Billing Determinants reflect DALs which were subject to the surcharge established in Docket No. R2006-1, or did the Postal Service start collecting data on DALs before the surcharge took effect on May 15, 2007?
- Since the Billing Determinants show an average revenue of 1.5 cents/piece on all 528.9 million of these DALs, is it correct to infer that the reported data reflect only paid DALs?
 - If the datum reflects only paid DALs (*i.e.*, volume entered after May 15, 2007), then (i) what was the total volume of DALs entered during the entire fiscal year, (ii) what volume was used to distribute city and rural carrier costs for the year, and (iii) from whence was that volume derived?
 - Again, if the reported datum of 528.9 million reflects only paid DALs (*i.e.*, volume entered after May 15, 2007), then when did the Postal Service actually start collecting data on DAL volume?

On May 15, or at some later date, *e.g.*, July 1, 2007?

For the period over which data were collected, what was the average monthly volume of paid DALs?

The type of information discussed here would be important to know because (i) the cost of handling billions of DALs mailed annually, when inappropriately charged to letters (as has

been done at times in the past (*see* Docket No. R2005-1, *Op. & Rec. Dec.*, ¶ 6077)), can skew the costing analysis badly, (ii) the initial rate for DALs established by the Commission was below cost, and (iii) data concerning DALs deserve to be recorded as accurately and systematically as they are for all other ratemaking components.¹⁸ Here again, analysis and explanation would be helpful, but there is none.

B. The Billing Determinants raise unanswered questions about saturation parcels and DALs

The Billing Determinants (USPS-FY07-4) show a total of 924,706 saturation parcels, with an average weight of 4.7669 ounces, which suggests that they would fit into typical mail boxes. To go with these parcels, 1,587,102 DALs are shown. DALs are required to be submitted with saturation parcels, which tend primarily to be product samples, hence the volume of saturation parcels and DALs would be expected to match exactly. (Further, all of the Saturation Parcels DALs are shown as pound-rated pieces, but the number of saturation pound-rated parcels is only 317,400.) No explanation is provided for the mis-match between the number of parcels and the number of DALs.

C. Billing Determinants for ECR letters

In the category of basic letters in ECR, 2.440 billion pieces are shown. Of these, 0.357 billion are shown as piece-rated, 0.000177 billion are shown as pound-rated letters (which appear to represent a category commonly referred to as heavy letters, weighing from 3.3 to 3.5 ounces each), 0.981 billion (40.2 percent of the total) are shown as being in a category labeled

¹⁸ The Commission discussed the issue of DALs extensively in the last rate case before setting the below-cost rate. *See* Docket No. R2006-1, *Op. & Rec. Dec.*, pp. 267-84.

as “Mixed,” and 1.102 billion are shown as automation letters (a category that was eliminated on May 15). “Mixed” categories also exist for high density and saturation letters, but do not exist for flats or parcels. It is not clear what this new “Mixed” ECR letter category represents, or how figures for this category should be used in rate development.

Since no procedure for discovery to the Postal Service currently exists in annual compliance review dockets, we would respectfully recommend that the Commission pose questions to the Postal Service regarding issues raised in this subsection.

V. PERIODICALS CONTINUE TO BE CROSS-SUBSIDIZED BY OTHER CLASSES DESPITE THE PRA AND PAEA REQUIREMENT THAT EACH CLASS COVER ITS ATTRIBUTABLE COSTS.

A. Periodicals rates continue to fail to cover costs and continue to be cross-subsidized by other classes of mail

Both PRA and PAEA **require** that each class of mail at a minimum cover its respective attributable costs. Former 39 U.S.C. section 3622(b)(3) required the Commission to issue a recommended decision on a Postal Service request for a rate change in accordance with several factors, including:

the **requirement** that each class of mail or type of mail service bear the **direct and indirect postal costs attributable** to that class or type plus that portion of all other costs of the Postal Service reasonably assignable to such class or type. [Emphasis added.]

Current 39 U.S.C. section 3622(c)(2) maintains precisely the same requirement, with the addition that postal costs be attributed “through reliably identified causal relationships”:

the **requirement** that each class of mail or type of mail service bear the **direct and indirect postal costs attributable** to each class or type of mail service through reliably identified causal relationships plus that portion of all other costs of the Postal Service reasonably assignable to such class or type. [Emphasis added.]

This is not a vague criterion which can be either tempered or disregarded depending on other circumstances, but a firm requirement imposed on both the Commission and the Postal Service. National Association of Greeting Card Publishers v. United States Postal Service, 462 U.S. 810, 820 (1983).

Nevertheless, for 11 consecutive years, Periodicals, as a class, has failed to cover its attributable costs, as demonstrated in Table I, below. And this also means, of course, that for 11 consecutive years, Periodicals has failed to contribute so much as \$1.00 toward the required “portion of all other costs of the Postal Service reasonably assignable to such class.” This is not a problem based on an anomalous cost in one or two studies, but based on costs and repeated over a decade.

Table I
Revenue, Cost, Coverage, and Cross-Subsidies to Periodicals

PRC CRA Year	Revenue (millions)	Cost (millions)	Coverage	Revenue-Costs (millions)
2007	2,187.9	2,635.6	83.01 %	-447.7
2006	2,124.8	2,487.6	85.42 %	-362.8
2005	2,068.9	2,431.6	85.08 %	-362.7
2004	2,100.0	2,323.3	90.39 %	-223.3
2003	2,139.6	2,196.2	97.42 %	-56.6
2002	2,066.9	2,280.4	90.64 %	-213.5
2001	2,106.9	2,367.1	89.01 %	-260.2
2000	2,076.3	2,354.8	88.17 %	-278.5
1999	2,017.7	2,213.1	91.17 %	-195.4
1998	1,972.8	2,129.0	92.66 %	-156.2
1997	1,964.6	2,038.5	96.37 %	-73.9
Total	22,826.4	25,457.2	89.67 %	-2,630.8

As can be seen, beginning in FY 1997, Periodicals has had cost coverages below 100 percent, ranging from 97 percent in 2003 to 83 percent in 2007. Cumulatively, the cross-subsidy of Periodicals by **other classes of mail** for this period has been \$2.6 billion. *See* Docket No. RM2007-1, Valpak Comments on Regulations Establishing a System of Ratemaking in Response to Commission Order No. 26, Sept. 24, 2007, p. 17.

The Postal Service Report shows that for FY 2007 the cost coverage of Periodicals is 83.01 percent, which added another \$447.7 million to the cumulative cross subsidy paid by all

other classes, primarily First-Class Mail and Standard Mail.¹⁹ (As noted elsewhere in these comments, the data for FY 2007 reflect two different sets of rates. For Periodicals, higher rates took effect on July 15, 2007. Revenues thus reflect lower rates that were in effect from Docket No. R2005-1 for nine and one-half months, and higher rates from Docket No. R2006-1 for two and one-half months.)

A brief analysis of these Periodicals data on revenues and costs indicates that revenues in the Periodicals class still may be failing to cover attributable costs, while other classes of mail continue to cross-subsidize Periodicals. First, starting with the FY 2007 data as reported, reflecting revenues from the “dual” set of rates discussed above, a coverage of 83.01 percent is indicated, as shown in Table A. The 83.01 percent coverage would require an increase in revenues of 20.5 percent in order to achieve 100 percent cost coverage. Second, observing that if the lower rates that were in effect until July 15, 2007 had remained in effect all year — *i.e.*, for the remaining two and one-half months — then revenues from Periodicals would have been less than the reported \$1.96 billion, while costs would have been little affected. Although this hypothesized reduction in revenues might have been small, it nevertheless would have been measurable. This means that under the Docket No. R2005-1 rates alone, an increase in revenues of even **more than 20.5** percent would have been necessary in order to achieve 100 percent cost coverage. For Periodicals, however, the average increase which took effect in

¹⁹ See USPS-FY07-1, Cost and Revenue Analysis.

July 2007 was estimated at only 11.8 percent.²⁰ This is well short of the requisite increase needed to achieve a breakeven coverage of 100 percent.

B. The Commission should require that the Postal Service set rates to ensure that Periodicals cover its costs

The Commission's review in this docket is authorized and governed by PAEA (39 U.S.C. § 3653). There is no question that in a conventional annual compliance review, the Commission must review each class of mail to ensure compliance with the 39 U.S.C. section 3622(c)(2) requirement that rates cover costs. However, the current annual compliance review is not fully conventional, but transitional, as the rates now under the Commission's review were set under PRA and the PRA ratemaking criteria (*see* discussion at Section II, *supra*). PAEA is silent on the Commission's power under a transitional annual compliance review. In this transitional case, it would appear that the Commission still has responsibility to determine if Periodicals rates in effect in FY 2007 were compliant with 39 U.S.C. section 3622(c)(2). However, PAEA must be examined carefully to determine what remedial powers the Commission would have in such a situation.

The PAEA section which grants the Commission remedial power is as follows:

(c) Noncompliance With Regard to Rates or Services. — If, for a year, a timely written determination of **noncompliance** is made **under subsection (b)**, the Postal Regulatory Commission **shall take appropriate action** in accordance with subsections (c) and (e) [sic] of section 3662 (as if a complaint averring such noncompliance had been duly filed and found under such action to be justified). [39 U.S.C. § 3653(c) (emphasis added).]

²⁰ Docket No. R2006-1, *Op. & Rec. Dec.*, p. iv.

In turn, the referenced “subsection (b)” provides that the compliance must be evaluated with respect to “applicable provisions of this chapter (or regulations promulgated thereunder). . . .”

When noncompliance is found, subsection (c) of the complaint section is triggered, and the Commission:

shall order that the Postal Service take such action as the Commission considers appropriate in order **to achieve compliance** with the applicable requirements and to remedy the effects of any noncompliance (such as ordering **unlawful rates to be adjusted to lawful levels**, ordering the cancellation of market tests, ordering the Postal Service to **discontinue providing loss-making products**, or requiring the Postal Service to make up for revenue shortfalls in competitive products). [39 U.S.C. § 3662(c) (emphasis added).]

A case could be made that PAEA requires that a Commission finding of noncompliance with PAEA (even if the rates originally were set under PRA) “shall” be accompanied by “appropriate action” by the Commission, “ordering unlawful rates to be adjusted to lawful levels.” However, Periodicals mailers could be expected to argue that a finding of noncompliance with subsection (b) would be illogical, as the rates originally were set under PRA, or perhaps that “appropriate action” in this case would be somewhat short of correcting the illegal pricing.

In the past, Periodicals mailers have anticipated such a day as this, and have seemed to argue that the “requirement” that rates cover costs was no more than precatory language. *See, e.g.*, Docket No. RM2007-1, Initial Comments of American Business Media (Apr. 6, 2007), pp. 3-4 (“To provide otherwise, and thus to permit excessive cost increases to obliterate the price cap, would be precisely the wrong message and would undermine what is likely the single most important provision of the PAEA.”) At least two mailers provided a method to

achieve the self-serving objective of perpetuating cross-subsidy. The Alliance of Nonprofit Mailers and Magazine Publishers of America, Inc. proposed a “solution” to the problem of a class of mail which did not cover its costs. *See* Docket No. RM2007-1, Comments of Alliance of Nonprofit Mailers and Magazine Publishers of America, Inc. on Advance Notice of Proposed Rulemaking (Apr. 6, 2007), p. 6. They proposed that rates for this class be increased at the maximum permitted under the cap until the losses were overcome, *i.e.*, until revenues started covering costs. But in view of the facts that (i) the cost coverage in FY 2007 was only 83 percent, (ii) at currently existing rates the revenue shortfall in FY 2007 exceeded 8.7 percent, and (iii) rate increases under PAEA reflect the general escalation in costs (as reflected by the CPI), the PAEA ratemaking system likely would need to be in effect for at least a decade — and perhaps far longer — before the cross-subsidy would be corrected under their approach.

No question exists, however, that under PAEA rates for each class must cover attributable costs. *See* Docket No. RM2007-1, Valpak Reply Comments on Regulations Establishing a System of Ratemaking in Response to Commission Order No. 2 (May 7, 2007), pp. 13-19, and Valpak Comments on Regulations Establishing a System of Ratemaking in Response to Commission Order No. 26 (Sept. 24, 2007), pp. 17-20. If the Commission were to determine in this annual compliance review that this “requirement” for revenues from each class cover their attributable costs does not trump the annual cap, then its only route for enforcing the requirement seemingly would be to order the Postal Service to focus the entirety of its rate increases, to the maximum extent feasible, on those cost drivers (and on those publications) that do not cover attributable costs. Such targeted rate increases typically would

be directed at those low volume, high-cost magazines that are circulated nationally.²¹ When the Postal Service files its Notice of Rate Adjustment with the Commission, the Commission will not be able to certify compliance with the 39 U.S.C. section 3622(c)(2) requirement as long as revenues from existing rates are less than the costs reported for FY 2007.²²

Respectfully submitted,

William J. Olson
 John S. Miles
 Jeremiah L. Morgan
 WILLIAM J. OLSON, P.C.
 8180 Greensboro Drive, Suite 1070
 McLean, Virginia 22102-3860
 (703) 356-5070

Counsel for:
 Valpak Direct Marketing Systems, Inc. and
 Valpak Dealers' Association, Inc.

²¹ This would reflect what many mailers from time to time have referred to as the realities of the marketplace. For instance, in Docket No. R2006-1, Initial Comment of American Bankers Association on the Reconsideration of Standard Mail Flats Rates (May 4, 2007) states that:

The new law [PAEA] intends that the Postal Service, in making ... pricing decisions, act more like a business.... By requiring the Postal Service to act more like a private business and operate under a price cap, Congress is seeking to force the postal system to become more efficient, **to eliminate cross-subsidies, and to ensure that the rates** that are charged actually track costs and comport with the **realities of the modern business environment**. [*Id.*, p. 2 (emphasis added).]

²² If the Postal Service were to agree with Periodicals mailers that rate increases for Periodicals cannot be made above the cap in a conventional rate case, it then would be compelled by PAEA to file an exigent rate increase, under 39 U.S.C. § 3622(d)(1)(E). *See* 39 C.F.R. § 3010.60-66.

Appendix A

Comparison of PRA Rate Case Filing and Annual Compliance Report (and 2007 Comprehensive Statement of Postal Operations)

PRC Rule 3001.54 (under PRA)	PAEA ACR Requirements (39 USC § 3652) (subsections specified below) (no regulations yet promulgated)	ACR2007 Report and Public Attachments (Library References), and 2007 Comprehensive Statement of Postal Operations	
(b)(1)	Schedules of then-effective rates and proposed rates	Analysis of rates (a)(1)	Report, pp. 7-14 (Analysis but no rates)
(b)(2)	Specifications of mailability and standards	Product information of MD products (a)(2)(A)	None
(b)(3)	Description of cross-elasticity of demand		Filing of Demand Analysis Material (Jan. 16, 2008)
(b)(4)	Identification of nonpostal services		N/A – See Docket No. MC2008-1
(c)	Identification of the characteristics of mailer and recipient and a description of the contents of items mailed at various subclasses		None
(d)	Physical attributes of the items mailed by subclass, including shape, weight, and distance		Mail Characteristics Study – FY07-14
(e)	Special service arrangements		None
(f)(1)	Total actual accrued costs for the most recent fiscal year	Analysis of costs (a)(1)	Report; pp. 7-14 Cost and Revenue Analysis (CRA) – FY07-1
(f)(2)	Estimated total accrued costs for the fiscal year in which the filing is made		N/A
(f)(3)(i)	(f)(1) and (f)(2) must show the costs in sufficient detail as to accounting and functional classifications so that they may be readily understood		Delivery Costs by Shape – FY07-19; Window service costs by shape – FY07-20; BPM processing costs and Parcel Post window services – FY07-22; mail processing costs by shape – FY07-26
(f)(3)(ii)	State and fully explain amounts for (a) depreciation on capital facilities and equipment; (b) debt service; (c) contingencies; and (d) extraordinary or nonrecurring expenses		Facility and Equipment Inputs – FY07-8
(f)(3)(iii)	Assign and distribute costs by cost segments and functions together with related mail volumes and to subfunctions and an explanation of the method of assignment/distribution	Information relating to workshare discounts: (1) per-item cost avoided; (2) percentage of such per-item cost avoided that the per-item workshare discount represents; and (3) the per-item institutional contribution (b)	Cost Segments and Components Report – FY07-2; Workshare discounts and passthroughs – FY07-3; Workshare Letter Costs – FY07-10; Workshare Flats Cost Models – FY07-11; Hybrid/Parcel Workshare Costs – FY07-12; Dropship Cost Avoidance – FY07-13; Parcels Workshare Cost – FY07-15; BPM, Parcel Post transportation costs, bulk parcel return workshare cost – FY07-16; Parcel Post cube weight relationship – FY07-17; ECR workshare analysis – FY07-18; QBRM Workshare costs – FY07-21
(g)	Total actual accrued costs since the most recent filing		CRA – FY07-1
(h)(1)	The separation of costs between postal and nonpostal including methodology		None

(h)(2)	Direct attributable costs, indirect attributable costs, costs reasonably assignable, and costs which cannot be attributed or assigned		Cost Segments and Components Report – FY07-2; MOD Productivity data – FY07-23; Non-operation specific piggyback factors – FY07-24; Operation specific mail processing piggyback factors – FY07-25
(h)(3)	Methodology of attribution or assignment		CRA Model – FY07-5
(h)(4)	Attribution shall be to classes, subclasses, special services, or rate categories with an analysis of the effect on volume, peaking patterns, priority of handling, mailer preparations, quality of service, physical nature, expected gains in productivity, and any other factor affecting costs		No changes to cost attribution being proposed as part of ACR2007 except for Periodicals addressed in two technical conferences
(h)(5)	Roll-forward model		N/A
(h)(6)	Attributable cost final adjustments by class, subclass, rate category, and service; details of the development and an explanation of each adjustment		None
(h)(7)	Other services adjustments		None
(h)(8)	An overall summary cost table		CRA – FY07-1
(h)(9)	For each cost segment, base-year amounts for each included account and sub-account shall be provided		IOCS statistical and computer documentation – FY07-27; CCCS statistical and computer documentation – FY07-28; RCCS statistical and computer documentation – FY07-29; TRACS statistical and computer documentation – FY07-30
(h)(11)	Clearly and separately identify any nonattributed or unassigned costs		None
(h)(12)	The data relevant to the analysis of the effect on costs specified in (h)(4)		See response to (h)(4)
(i)	Statement of criteria employed in constructing the proposed rate schedule		N/A
(j)(1)	actual and estimated revenues for the fiscal years selected for (f) and (g) using before rates	Analysis of revenues (a)(1)	Report, pp. 7-14; CRA – FY07-1
(j)(2)	estimated revenues based on proposed rates for fiscal year selected for (f)(2)		N/A
(j)(3)	actual and estimated revenues shown in (j)(1) and (2) disaggregated by class, subclass, each unique rate element, and postal service		CRA – FY07-1
(j)(4)	documentation of (j)(1)-(3) sufficient to allow independent replication, with references to data sources		CRA "B" Workpapers – FY07-6; Cost Segment 3 Cost Pools – FY07-7
(j)(5)(i)	an econometric demand study by class and subclass		Filing of Demand Analysis Material (Jan. 16, 2008)
(j)(5)(ii)	actual and estimated volumes at current rates beginning with the last complete fiscal year and ending with the last full future year	Mail volumes of MD products (a)(2)(A)	CRA – FY07-1; Billing Determinants – FY07-4; N/A for future years under PAEA

(j)(5)(iii)	estimate volumes at the proposed rates beginning with the quarter when the rates are assumed to be effective and ending on with the last full future year		N/A
(j)(6)	Supporting rationale for forecasted volumes and revenues, including computer implementation		N/A
(j)(7)	All of the input files need to replicate the econometric demand study, price indices, used to prepare the data for use in the econometric demand study		Filing of Demand Analysis Material (Jan. 16, 2008)
(k)(1)	For the two preceding complete fiscal years the Balance Sheet, the Statement of Income and Expense, basic statistical information and the Statement of Income and Expense by budget categories (and supporting schedules)		Competitive Products Contribution – FY07-9; under PAEA, USPS Annual Reports available on-line
(k)(2) and (3)	A reconciliation of the budgetary information with actual accrued costs for the most recent fiscal year (or preliminary or pro forma information if actual not fully available on the filing date)		None
(l)	Billing determinants		Billing Determinants – FY07-4
(m)	Continuing and phasing appropriations		None
(n)(1)	Performance goals	Analysis of quality of service (a)(1)	Report, pp. 14-17 (Section II.C)
(n)(2)	Achieved levels of service for those classes/subclasses and services for which performance goals have been set	Measures of the quality of service of MD products including (1) level of service (speed of delivery and reliability) provided and (2) degree of customer satisfaction (a)(2)(B)	Report, pp. 14-19 (Section II.C - II.D.)
Rule 53(b)	Overview of filing		Roadmap – FY07-31
		Market Test information, including costs, revenues, quality of service, and such other data as the PRC requires (c)	None
		Working papers and any other supporting matter that the PRC shall prescribe (d)	N/A
		Comprehensive Statement under § 2401(e) (g)(1)	2007 Comprehensive Statement on Postal Operations (filed Jan. 11, 2008)
		Performance plan under § 2803 (g)(2)	2007 Comprehensive Statement on Postal Operations (filed Jan. 11, 2008)
		Program performance report under § 2804 (g)(3)	2007 Comprehensive Statement on Postal Operations (filed Jan. 11, 2008)